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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1938.

No. 53

In the Matter of
TAX SERVICE ASSOCIATION OF ILLINOIS,
Alleged Bankrupt.

ROY G. HARRIS and BENJAMIN F. J. ODELL,
Petitioners,

vs.

AVERY BRUNDAGE COMPANY, et al., and DAHLSTEDMAN CO., et al.,
Respondents.

BRIEF FOR PETITIONERS

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BRIEF FOR PETITIONERS

OPINIONS BELOW.

The orders of the District Court of the United States for the Northern District of Illinois, Eastern Division (Rec. 96, 99) have not been reported.

The opinion (Rec. 129) of the Circuit Court of Appeals is reported in 95 Fed. (2d) 373.

JURISDICTION.

The orders of the District Court appealed from, as aforesaid, were entered July 12th and 13th, 1937, respectively, (Rec. 96, 99). Appeal was denied in the District Court but was allowed by the Circuit Court of Appeals for the Seventh Circuit September 11, 1937.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, (C 229, Sec. 1-43, Stat., 938, 28 U. S. C. A. Sec. 347 (a)), also under Rule 38 of this Court.

The date of the judgment to be reviewed is March 9, 1938, (Rec. 129). Petition for rehearing was denied April 14, 1938, (Rec. 197). Certiorari to the Seventh Circuit was granted by this court May 31, 1938.

STATEMENT OF THE CASE.

This is an appeal from orders of the District Court in an attempted bankruptcy proceeding, resisted by alleged bankrupt as a non-profit corporation. The order directed that the sum of $48,580, out of a $72,000 escrow fund held by three trustees be turned over to an alleged committee, as interveners, (the respondents herein).

The escrow fund, the balance of which is now in controversy, arose in this manner: Petitioner Odell is an attorney with considerable experience in sales tax matters. Several hundred building contractors' through various trade associations, sought Odell's service and requested him to represent them in obtaining a construction favorable to them with respect to their sales tax liabilities under the Illinois Retailers' Occupation Tax Act, commonly known as the Sales Tax Act.

Odell expressed his willingness to represent the various contractors, but on condition that some arrangement be made whereby he would be relieved of the heavy burden of purely clerical details and labor incident to such an undertaking. Thereupon the various trade associations procured the alleged bankrupt, Tax Service Association, of which some of the associations and individual contractors were members, to handle these details, and entered into a written agreement with Tax Service Association agreeing to pay the said association $1,500 for clerical services, and designating the manner in which the payment of Odell's fee should be apportioned among the various contractors and, incidentally, limiting the expense to which the various contractors should be subject in the aggregate to $15,000 or $20,000, depending on how far the litigation was carried. The trade associations notified Odell of this arrangement and later the individual contractors engaged Odell by individual written contracts (Appendix *infra* and also Rec. 25). Following the separate engagement of Odell by all of the contractors individually, he approved the agreement between the contractors' associations and the Tax Service Association.

Pending determination of this legal issue, and to pave the way for an interlocutory injunction restraining the taxing authorities, it was decided to escrow the taxes claimed by the State of Illinois as they accumulated. On May 2, 1935, Harris and Odell, petitioners herein, and the third escrowee or trustee, E. M. Craig, directed a letter to the National Builders Bank of Chicago, calling the attention of the bank to the opening of an account for the contractors in that bank entitled Sales Tax Escrow Fund (Rec. 27). The letter stated that the funds were in the custody and control of these three pending the outcome of proposed negotiations with the Department of Finance of

the State of Illinois, and the letter contained directions that the funds were to be paid out only on signatures of the three escrowees, Craig, Harris and Odell, or their alternates, whose names appeared in the letter.

The identity and relations of these escrowees have become significant. E. M. Craig was the secretary of the said various trade associations and in no way connected with the alleged bankrupt. Odell was the contractors' attorney. R. G. Harris was a vice president of the alleged bankrupt.

Negotiations with the Department of Finance being unsuccessful, the contractors, through their attorney Odell, instituted a suit in the Circuit Court of Cook County for the purpose of obtaining a construction of the said Tax Act. This bill filed by the contractors, was dismissed for want of equity. The contractors then appealed to the Supreme Court of the State of Illinois. The Supreme Court deciding partially in their favor, reversed the decision of the Circuit Court of Cook County and remanded the cause (Rec. 51, *Blome Co.* v. *Ames*, 365 Ill. 456, 459). In conformity with the decision of the Supreme Court, the Department of Finance of the State of Illinois was compelled to change its ruling and extend unqualified exemption from the Sales Tax on labor furnished by contractors, which it had not conceded theretofore (Rec. 161).

Subsequently, the Illinois Supreme Court voluntarily modified and extended its said decision on the said *Blome* case (Rec. 163, *Herlihy Mid-Continent Co.* v. *Nudelman*, 367 Ill. 600, 605) and held that the contractors were not liable for Sales Taxes on either labor or materials, but completely exempt therefrom. As a result of the efforts of Odell, their attorney, the contractors are now exempt from the tax and entitled to refunds from the State of Illinois, estimated at hundreds of thousands of dollars, as

provided by special refund provision of the Act. Smith Hurd Illinois Annotated Statutes, Chap. 120, Sec. 445. (Appendix *infra*).

On May 3, 1937, an involuntary petition in bankruptcy was filed against the Tax Service Association of Illinois. The said association resisted the petition upon the ground that it was a "not for profit corporation", and that the court had no jurisdiction to entertain an involuntary petition because the corporation was not a "moneyed, business, or commercial corporation" within the purview of the Bankruptcy Act; denied it was insolvent; denied that it had committed any acts of bankruptcy; and denied that there were sufficient creditors (Rec. 77). Up until the time of decision of this case in the Circuit Court of Appeals, there had been no adjudication, although adjudication has since followed.

On May 24, 1937, there was in excess of $314,000 in the said escrow fund, and at that time said interveners filed an intervening petition in the said bankruptcy proceeding, making the three escrowees, the alleged bankrupt, the bankruptcy receiver and the bank, respondents (Rec. 18), alleging in substance that most of the said money belonged to interveners and requested its return (Rec. 28); that the money was under the control of Harris and Odell (Rec. 31-2); that Harris and Odell were requested to cease acting as agents of interveners but had refused (Rec. 32); that none of the money belonged to the alleged bankrupt and asking that the three escrowees be compelled to sign a check turning over the funds to interveners, an alleged committee of three, and that the bank be compelled to honor the check.

Immediately after the filing of the said intervening petition, it became imperative to turn over 75% of the escrow fund to the Department of Finance of Illinois in

order to avoid impending heavy penalties to the contractors. (Seven months later this amount was held not due as a tax.) For the purpose of avoiding this penalty to interveners an "agreed" order, was entered May 27, 1937, turning over 75% of the said money in the escrow fund to the Department of Finance of the State of Illinois (Rec. 39). The 75% was a compromise figure (representing a tax on material only) made with the State of Illinois for said contractors (interveners) and many other contractors who had deposited their taxes in said escrow fund, the latter contractors not being parties to this proceeding. In said order Harris and Odell were given until June 3, 1937, to file their answers or other pleadings to the intervening petition, and on that day they, as well as the alleged bankrupt, filed a motion to strike said petition for want of jurisdiction of the court to determine any rights in the fund (Rec. 54-57). The said National Builders Bank answered reserving the right to object to the entry of orders for payment in any form other than by the agreement under which the funds were deposited (Rec. 46). The bankruptcy receiver in his answer maintained that the litigation, by Odell, for the contractors was successful, and that $20,000 of the said fund should be held until adjudication (Rec. 51-53). There was no further hearing on the said intervening petition, or the above-mentioned motions to strike or answers filed in opposition thereto.

On June 29, 1937, the intervening committee abandoned its said petition and filed another petition in which it asked that $48,580.40 be turned over to them, exclusive of $20,000, which the receiver requested be held pending adjudication (Rec. 69). The above motions of Harris and Odell, to strike, were again urged to the second petition and the question of jurisdiction was referred to a referee (Rec. 73).

On the afternoon of the same day counsel for interveners (respondents) presented a purported order which was signed by the court without the presence, knowledge or consent of other counsel in the case, which order purported to indicate that the court had directed Harris and Odell to answer the petition, and that each of them had thereupon stated that he did not desire to answer said petition and further recited that he desired to stand upon the jurisdictional question theretofore raised (Rec. 74). This part of the order was not true; at no time did either Harris or Odell, petitioners here, state that he did not desire to answer said petition. In fact they merely stated that they desired to raise first the question of jurisdiction (Rec. 92).

On July 7, 1937, the referee recommended that the interveners' request be allowed, and that the sum of $48,580.40 be paid to the intervening committee (Rec. 78) despite the fact that the reference to him and the issue before him were solely on the one question of jurisdiction. The court, over objections, allowed petitioners here two days to file exceptions to the report, in violation of rules granting 10 days, or 20 days if the referee was a special master. These petitioners asked for an extension of time to file exceptions, which leave was denied them (Rec. 92). Exceptions inadequately drawn were filed which called the attention of the court to the erroneous language in the order of reference, and the surreptitious manner in which that order was obtained by counsel for interveners (now respondents) (Rec. 92-5). Petitioners then immediately asked leave to file an answer to the merits, which leave was denied them (Rec. 96). An order was then summarily entered overruling exceptions, approving the referee's report, and directing these petitioners to sign a check for $48,580.40 in favor of the intervening so-

called special committee (Rec. 96). The next day the court granted interveners' (respondents) motion to strike the special answers theretofore filed by petitioners here to the jurisdiction (Rec. 100).

The District Court subsequently denied petitioners here leave to appeal. Appeal was later granted by the Circuit Court of Appeals. That court affirmed the orders of the District Court.

SPECIFICATIONS OF ERRORS.

The Circuit Court of Appeals erred:

1. In permitting the bankruptcy court to assume jurisdiction over funds and controversies not involved in the bankruptcy estate.

2. In permitting the bankruptcy court to assume jurisdiction over a fund in litigation which was not in the control or custody of the alleged bankrupt or of the court.

3. In holding that jurisdiction over the subject matter was conferred by consent, or could be conferred by consent.

4. In permitting the bankruptcy court to entertain an intervening petition foreign to the bankruptcy proceeding.

5. In finding that the escrow fund was closely connected with the affairs of the alleged bankrupt, or was under the control of the alleged bankrupt and was, therefore, in *custodia legis*.

6. In holding that mere constructive possession is sufficient to sustain a reclamation proceeding.

7. In permitting the trial court to try collateral issues

prior to determination of question of jurisdiction over the alleged bankrupt.

8. In not dismissing the controversy because of lack of jurisdiction over the alleged bankrupt.

9. In sanctioning the action of the trial court in arbitrarily restricting the time for the filing of exceptions to the referee's report, and refusing an extension thereof, all in violation of rules.

10. In sanctioning the action of the trial court in not dismissing the petition as required by statute when lack of jurisdiction apparent on face of the petition, was called to its attention.

11. In sanctioning the arbitrary denial by the trial court of these petitioners' rights to plead to the merits, after a plea to the jurisdiction had been decided unfavorably to them.

12. In finding that Harris and Odell were acting as agents of the alleged bankrupt in serving as trustees of the funds in litigation.

13. In finding that the litigation with respect to the Illinois Sales Tax was unsuccessful when that question was pending unheard, undetermined upon pleading of non-appealing parties in the court below, and the contrary was true in fact.

14. In finding that these petitioners neglected or refused to plead to the merits when the record shows that they asked for and were denied opportunity so to plead after the overruling of their jurisdictional pleas.

15. In making findings of fact with respect to a balance of a certain fund which was not the subject matter of appeal.

16. In taking jurisdiction over disputed funds involved in pending injunction in a state court.

SUMMARY OF ARGUMENT.

POINT I. The court of bankruptcy did not have jurisdiction to enter the orders appealed from.

1. This controversy was not a bankruptcy controversy but one between strangers to the bankruptcy proceeding.

2. This litigation constitutes neither a proceeding in bankruptcy nor a controversy arising out of bankruptcy and hence cannot be cognizable by a court of bankruptcy.

3. The escrowees were not agents for the alleged bankrupt nor were they subject to its control.

4. There was neither actual nor constructive possession within the meaning of such terms as used by the authorities.

5. Mere constructive possession is not sufficient to confer upon the bankruptcy court jurisdiction over a reclamation suit.

6. The petitioners here did not, in fact consent to the jurisdiction of the bankruptcy court.

7. Consent cannot confer jurisdiction of subject matter, *i. e.*, jurisdiction on the bankruptcy court of a controversy between strangers to the bankruptcy proceeding.

POINT II. The orders appealed from deprived these petitioners of property without any opportunity whatever to be heard on the merits of the issues.

POINT III. The Circuit Court of Appeals and the Trial Court commimtted further errors requiring reversal.

1. The court erred in entertaining an involuntary petition against a corporation organized not for profit.

2. The court erred in determining an intervening controversy when its jurisdiction over the bankruptcy proceeding was in issue and undetermined.

3. The court disregarded Equity Rule 66 and denied sufficient time to file exceptions to the Special Master's Report.

FOREWORD.

In view of the extraordinary situation here, your petitioners crave the initial attention of the Court to one or two phases, in the light of which it is asked that all aspects of the present controversy be viewed. First, the facts developed in the trial court were *ex parte* facts of interveners alone. Petitioners did not have an opportunity to be heard, and present their facts. Second, the assumption of jurisdiction by the bankruptcy court was not merely caused by ordinary error or oversight; the assumption and retention of such jurisdiction was brought about by the deliberate contrivance of the interveners to create certain false appearances and indicia of jurisdiction, *e. g.*, by joining the receiver as defendant to suggest some connection with the bankrupt estate, and also by the entry of the "agreed" order of May 27th, 1937.

ARGUMENT.

Point I.

The court of bankruptcy did not have jurisdiction to enter the orders appealed from.

At the outset petitioners are at a tactical disadvantage in arguing to the jurisdiction, in that neither the bankruptcy court, nor the Circuit Court of Appeals, nor the respondents have at any stage of the proceedings enunciated clearly the theory upon which the fundamental jurisdiction of the bankruptcy court was predicated. That the jurisdiction must be bankruptcy jurisdiction is apparent, inasmuch as the intervening petitions were filed in the bankruptcy court, and inasmuch as no diversity of citizenship, federal question, or any other possible basis for federal jurisdiction is anywhere suggested in the pleadings, evidence, or orders of the court. In view of the limited nature of bankruptcy jurisdiction, it would seem incumbent upon those depending upon it to indicate the basis therefore.

The Circuit Court of Appeals devotes approximately a page and a third of its opinion to the problem of jurisdiction; which it characterizes as "the essential question presented" (Rec. 132). A portion of the opinion would indicate that the court regarded the proceeding as one for reclamation. Inasmuch as the opinion of the Circuit Court of Appeals seems to summarize the position of respondents, and we may assume, that of the bankruptcy

court, we direct brief attention to the portion of that opinion dealing with the subject of jurisdiction:

> "The essential question presented by the appeal is whether the court had jurisdiction to disburse the controverted fund * * *. It seems to us, even though it has been finally determined the bankrupt had no interest in the escrow fund, that the same was so closely connected with its affairs in that it was controlled and in the custody of its officers and agents, that the court properly acquired jurisdiction of the fund. If we be wrong in this view, however, the agreed order of May 27, 1937, expressly conferred jurisdiction * * *.
>
> "It is insisted, however, by appellants, that jurisdiction cannot be conferred by consent. Many cases are cited in support of this contention, but we think they are distinguishable from the situation here. As was said in *Page* v. *Arkansas Natural Gas Corporation*, 53 F. (2d) 27, on page 33 * * *" (Rec. 132).

The court then quotes a rather long dictum from said *Page* case to the effect that constructive possession confers jurisdiction.

It will be noted in case at bar that although the court purported to set out the consent theory as an alternative ground of jurisdiction, the court meets the argument that jurisdiction cannot be conferred by consent by its return to the constructive possession theory of the *Page* case. Clearly the court declined to attempt to sustain the consent argument independently.

For the Circuit Court of Appeals to render the decision it did in this case, it was necessary for it to endorse the erroneous contentions of law and fact made by interveners in the District Court. These erroneous assumptions are:

1. That the proceeding involved bankruptcy litigation and was not between strangers to the bankruptcy proceeding.

2. That this litigation constituted either a proceed-

ing in bankruptcy or a controversy arising out of bankruptcy.

3. That the three escrowees were merely agents for the alleged bankrupt, and under its control.

4. That there was either actual or constructive possession within the meaning of those terms as used in the cases relied upon.

5. That mere constructive possession is sufficient to confer upon the bankruptcy court jurisdiction of a reclamation suit. (An obvious failure to distinguish between "reclamation" proceedings and "turnover" proceedings.)

6. That the appellants consented to the jurisdiction of the bankruptcy court.

7. That consent can confer jurisdiction of subject matter, *i. e.*, confer jurisdiction on the bankruptcy court over a controversy between strangers to the bankruptcy proceeding.

1.

The controversy was not a bankruptcy controversy but one between strangers to the bankruptcy proceeding.

Neither petitioners nor respondents were parties to the bankruptcy proceeding. Omitting irrelevant details the facts were these:

Four alleged creditors filed an involuntary petition in bankruptcy against a taxpayers association organized under the laws of the State of Illinois as a not-for-profit corporation. The corporation contended in good faith that it was not bankrupt and that anyway it could not be adjudicated an involuntary bankrupt.

A committee of three *claiming* to represent some two hundred building contractors, utter strangers to the bankruptcy proceeding, sought to intervene. The sole object in intervening was to obtain possession of funds

deposited, long prior to the bankruptcy proceeding, with three escrow officers or trustees for a purpose which had no connection whatever with that bankruptcy proceeding. The escrowees or trustees from whom they sought to obtain the funds were likewise strangers to the bankruptcy proceeding.

The general principle herein applicable with respect to jurisdiction is clearly enunciated in *Remington on Bankruptcy*, Fourth Edition (1936), Vol. V, Par. 2191:

> "Nor may third parties resort to the bankruptcy court to litigate their rights there, where neither the bankruptcy court has custody of the property, nor either of the parties was a party to the proceedings in bankruptcy, nor any property is recoverable by general creditors. * * *"

In the much followed case of *Nixon* v. *Michaels*, 38 Fed. (2d) 420 (8th Circuit, followed in several circuits), a case in which an intervening petitioner attempted to have the bankruptcy court direct the holder of a check—proceeds of a sale of bankruptcy assets—to turn the same over to the petitioner therein, the court in holding that the bankruptcy court had no jurisdiction (a question raised for the first time on appeal) said, on page 423:

> "But, leaving out of consideration preferential and fraudulent transfers, unless there is involved a *res* in the possession of the bankruptcy court, and in which *res* as a part of the bankrupt estate third parties claim rights, the bankruptcy court has no jurisdiction to allow such third parties to come into the bankruptcy court merely to litigate therein rights even against parties to the bankruptcy proceeding, and even though the property involved may once have been part of the bankrupt estate. Remington on Bankruptcy (3rd Ed.), Paragraphs 2191, 2199; *Henrie* v. *Henderson, supra; in re Hollins, supra; in re Girard Glazed Kid Co.* (D. C.), 136 F. 511; *in re Swofford Bros. Dry Goods Co.* (D. C.), 180 F. 549, 557; *in re Siegel* (C. C. A.) 256 F. 226."

Also in the case of *Henrie* v. *Henderson*, 145 Fed. 316 (4th Circuit, certiorari denied, 206 U. S. 563) where a somewhat similar situation arose, the court said at page 320:

> "* * * The object of the bankruptcy law is to afford the means by which the creditors of the bankrupt may secure an equitable and fair distribution of the bankrupt's property, etc., and the act contemplates that any collateral questions growing out of the settlement of the bankrupt's estate may be heard and determined in that court. But here we have parties who are contending about a matter which is in no way related to or connected with the affairs of the bankrupt. Under these circumstances, we fail to understand the theory on which this proceeding was instituted."

Possession of the subject matter of a controversy in the bankruptcy court becomes material only when there is a dispute between a bankruptcy trustee and a claimant of property which is, or which is claimed to be, the *estate of the bankrupt*. In such cases the Bankruptcy Act grants jurisdiction as follows:

> "(7) cause the *estates of bankrupts* to be collected, reduced to money and distributed, and determine controversies in relation *thereto*, except as herein otherwise provided;"
>
> United States Code, Title 11, Chap. 2, Sec. 11.

Clearly jurisdiction to determine controversies must relate to the *estate of the bankrupt*, and must bear some relationship to the subject of bankruptcy and the purpose of the bankruptcy act. That purpose has been clearly defined by this court in the case of *Williams* v. *U. S. Fidelity Co.*, 236 U. S. 549, on page 554; 59 L. Ed. 713, 35 Sup. Ct. Rep. 283, 34 A. B. R. 181, as follows:

> "It is the purpose of the Bankrupt Act to convert the assets of the bankrupt into cash for distribution

among creditors and then to relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortune. * * *"

The decision of the Circuit Court of Appeals, in case at bar, is in conflict with a decision of this court in the case of *Fulton Bank* v. *Hozier*, 267 U. S. 276 at 280 and 281. In that case an intervener sought to have the bankruptcy court recover property from a third person for his benefit. This court said:

"The general rule is that when a federal court has properly acquired jurisdiction over a cause it may entertain, by intervention, dependent or ancillary controversies; but no controversy can be regarded as dependent or ancillary unless it has a direct relation to property or assets actually or constructively drawn into the court's possession or control by the principal suit. * * *"

"* * * He had no right to bring the bank, which for jurisdictional purposes was to be deemed a citizen of Georgia (Jud. Code § 24, Subdiv. 16), into the Federal Court or to interfere with the affairs of the estate by injecting this controversy concerning which the receivers had no material interest—wherein the estate might lose much but could gain nothing."

It is submitted that under no circumstances could the dispute between petitioners and respondents be characterized as relating to the estate of the alleged bankrupt. The fund in litigation never was any part of the bankrupt estate. Neither the bankrupt nor the receiver, nor any creditor of the bankrupt, had claimed any interest in it. Neither petitioners nor respondents are, or claim to be, creditors of the alleged bankrupt.

As was said in *Nixon* v. *Michaels*, 38 Fed. (2d) 420, at 423-424:

"And, even if there be a *res* in the bankruptcy

court, it does not follow that it may be reached by a third party—a stranger to the bankruptcy proceedings. Thus it is held that the bankruptcy court has no jurisdiction to entertain a garnishment proceeding where a third party seeks to attach a dividend which has been declared by the trustee * * *. *In re American Elec. Tel. Co.*, (C. C. A.) 211 Fed. 88 * * * See also * * * *In re Argonaut Shoe Co.* (C. C. A.) 187 Fed. 784."

The subject matter of the case at bar is cognizable in equity only. The petition is in the nature of a bill against third parties for accounting and for specific performance. It involves numerous complicated questions of law and fact. Such litigation may extend over a period of years. Certainly the estate is not interested and the administration of its affairs should not be so burdened or hampered.

The present controversy, being one between strangers to the bankruptcy proceeding and over a fund in no sense part of the bankruptcy estate, is not cognizable in a court of bankruptcy.

2.

This litigation constitutes neither a proceeding in bankruptcy nor a controversy arising out of bankruptcy and hence cannot be cognizable by a court of bankruptcy.

As was said in *Bardes* v. *Hawarden Bank*, 178 U. S. 524, 531:

"In *Lathrop* v. *Drake*, (1875), 91 U. S. 516, the jurisdiction conferred on the District Court and the Circuit Courts of the United States by the Bankrupt Act of 1867 was defined by this Court, speaking by Mr. Justice Bradley, as consisting of 'two distinct classes first, jurisdiction, as a court of bankruptcy, over the proceedings in bankruptcy, initiated by the petition, and ending in the distribution of assets amongst the creditors, and the discharge or

refusal of a discharge of the bankrupt; secondly, jurisdiction, as an ordinary court, of suits at law or in equity, brought by or against the assignee in reference to alleged property of the bankrupt, or to claims alleged to be due from or to him." * * *

That this distinction between proceedings in bankruptcy and controversies arising out of bankruptcy has been preserved in the Act of 1898 has been consistently held by this court:

Bardes v. *Hawarden Bank*, 178 U. S. 524.

First National Bank v. *Chicago Title & Trust Co.*, 198 U. S. 280.

Schumacher v. *Beeler*, 293 U. S. 367.

Omitting subsection 7 of Section 2 of the Bankruptcy Act, it is so clear that the present litigation cannot possibly come within any of the other provisions of the said Section 2 that argument in support of that proposition is unnecessary. Subsection 7 of Section 2 is as follows:

"cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided;"

(The word "thereto" refers to the estates of the bankrupt as has been demonstrated in our argument immediately proceeding.)

It is clear that the words "except as herein otherwise provided" refer to Section 23 of the Act, as this court has held in *Bardes* v. *Hawarden Bank*, 178 U. S. 524, 529, and reiterated in *First National Bank* v. *Chicago Title & Trust Co.*, 198 U. S. 280, 289.

Section 23 of the Act is as follows:

"(a) The United States district courts shall have jurisdiction of all controversies at law and in equity,

as distinguished from proceedings in bankruptcy, between trustees as such and adverse claimants concerning the property acquired or claimed by the trustees, in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

(b) Suits by the trustee shall be brought or prosecuted only in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section 96, subdivision b, of this title; section 107, subdivision e, of this title; and section 110, subdivision e, of this title."

30 Stat. 552.

United States Code, Title 11, Chap. 4, Sec. 46.

Section 23 deals solely with controversies to which the trustee is a party. In the present litigation no trustee had been appointed; hence no jurisdiction could be predicated upon Section 23.

It seems clear that except for Sections 60b, 67e, and 70e, all dealing with suits by trustees, that Section 23 was intended by Congress as an exclusive treatment of controversies cognizable by courts of bankruptcy. In *Schumacher* v. *Beeler*, 293 U. S. 367, this court said at page 374:

"In enacting Section 23, it was clearly the intent of the Congress that the federal courts should not have the unrestricted jurisdiction of suits between trustees in bankruptcy and adverse claimants which these courts had exercised under the broad provisions of Section 2 of the Act of 1867. The purpose was to leave such controversies to be heard and determined for the most part in the state courts 'to the greater economy and convenience of litigants and witnesses.' But no reason appeared for a denial of

jurisdiction to a federal court if the defendant, the adverse claimant, consented to be sued in that court. * * *"

(The consenting defendant referred to is, of course, a defendant in a suit brought by a trustee.)

Conceivably it might be argued that since the statute refers to cases in which trustees are parties, that the bankruptcy court may have some broader jurisdiction with respect to controversies arising out of a bankruptcy to which the trustee is not a party. However, the fallacy of such an argument becomes apparent when considered in the light of the above-indicated purpose of Congress to limit the bankruptcy jurisdiction, and in the light of the logical improbability that Congress should intend to confer a broader jurisdiction in the absence of, than in the existence of a trustee, and in the light of the extremely limited powers of receivers in bankruptcy:

"(3) appoint receivers or the marshalls, upon application of parties in interest, in case the courts shall find it absolutely necessary for the preservation of estates, to take charge of the property of bankrupts after the filing of the petition and until it is dismissed or the trustee is qualified;"

United States Code, Title 11, Chap. 2, Sec. 11, (3).

The more logical conclusion to be drawn from the fact that provision is made only for controversies to which the trustee is a party, is that the Congress contemplated and intended that there might be such controversies, *only* when there was a trustee. There had been no trustee appointed in the present case as there had been no adjudication, and hence there could be no jurisdiction at all.

Assuming, however, solely for the sake of argument, that the term "trustee" as employed in Section 23 could by some possibility be metamorphosed into "representative of the estate", it would still follow that there could be no jurisdiction in the bankruptcy court. If Section 23a be sought to be invoked, it provides that the "District Courts shall have jurisdiction * * * in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants." It is clear that under such circumstances the District Court would have jurisdiction only if there were a diversity of citizenship, federal question, or some other independent ground of federal jurisdiction. It is, of course, nowhere even suggested that any such independent ground of federal jurisdiction exists.

If the consent provision of Section 23b be sought to be invoked, respondents are equally frustrated. Section 23 (b) refers only to proceedings brought *by* trustees, and not to proceedings *against* them. This court said in *Schumacher* v. *Beeler*, 293 U. S. 367, at the bottom of page 374:

> "* * * Exercising that power, the Congress prescribed in Section 23 (b) the condition of consent on the part of the defendant sued by the trustee. Section 23 (b) was thus in effect a grant of jurisdiction subject to that condition."

A controversy brought against a trustee or "representative of the estate" would be subject to the requirements of Section 23 (a), and would so require independent grounds of federal jurisdiction, unless it were a reclamation proceeding, in which event the jurisdiction of the bankruptcy court would lie without reference to the bankruptcy act and would arise from the *actual* pos-

session of the bankruptcy court, and from the fact that it alone could enable such complaining party to secure the property he claims. (The theory of such reclamation jurisdiction is treated later in this brief at page 30.)

The law is well settled that where an adverse claim is disclosed, the court has no jurisdiction to determine a controversy in a summary manner or proceeding. That there was such an adverse claim seems too clear to be disputed. One of the dominant elements in this entire case, and one to which the courts below have simply closed their eyes, is that this was an *escrow* and not a mere agency. Escrowees are trustees; not mere agents.

In the case of *Seibel* v. *Higham*, 216 Mo. 121, 132; 115 S. W. 987, the court said:

> "* * * The depositary of an escrow is sometimes spoken of as an agent of the grantor and sometimes as the agent of both parties, and whilst that may be correct, in a limited sense, yet strictly speaking he is not an agent at all, he is a trustee of an express trust, with duties to perform for each which neither can forbid without the consent of the other. If he were the agent of the grantor his agency would cease on the grantor's death and he would have no authority to receive the purchase money from the grantee and deliver the deed. But the death of the grantor does not annul the depositary's authority to do what he was appointed to do and it does not impair the right of the grantee to perform the condition and take down the deed. * * *"

It may be conceded, the fact that the letter controlling the fund referred to it as an escrow, and that all parties referred to it as such, is not necessarily conclusive that it was such in fact; but there can be no doubt that it was an escrow when the surrounding circumstances are considered. Had the money been held

merely by agents and not by escrowees or trustees, there would have been no purpose in having such a fund at all. If no one was intended to be given any interest in the fund other than the depositing contractors, why was not the money left in the individual bank accounts of the individual depositors? Obviously the money was held by the escrowees as trustees subject to rights of themselves and third parties. What these rights were does not appear clearly from the record, since there was no hearing concerning them, as hearing on the merits was denied. However, *what* they were is not important; what matters is *that they existed*. That one of these rights was a right of Odell to compensation would have been shown had opportunity been so given, is demonstrated hereafter. (Brief 52.) Actually the present proceeding is one for an accounting. Certainly no argument is required to show that an accounting suit against a trustee is an adverse proceeding. This proceeding should have been brought by complaint in chancery in the State Court.

The intervening petition constituting neither a proceeding in, nor a controversy arising out of, bankruptcy, authorizes no jurisdiction for the court.

3.

The escrowees were not agents for the alleged bankrupt nor were they subject to its control.

The decision of the Circuit Court of Appeals on the point of jurisdiction was based primarily on the theory that the alleged bankrupt had possession and custody of the fund in litigation, which is in turn founded upon the idea that Craig and these petitioners (the three escrowees) were mere agents of the alleged bankrupt.

Hence, the question of whether or not these escrowees were agents and under the control of the Tax Service Association becomes of paramount importance.

It is axiomatic that a principal can remove and replace an agent unless the agency is coupled with an interest.

Respondents contended (Rec. 28) and the Circuit Court of Appeals has found (Rec. 132) that none of the escrowees had any interest in the fund. Hence, under the law enunciated and their contention, the respondents and the Circuit Court of Appeals are forced to the fallacious position that the Tax Service Association could have removed and replaced any of the escrowees at will—that the Tax Service Association could have appointed other escrowees the day following the establishment of the escrow and caused the funds to be transferred to the account of the association itself. Would respondents or the Circuit Court of Appeals seriously attempt to support such a position as this in view of the letter controlling the escrow (Rec. 27) which specifically designated alternates (thus by implication excluding any other mode of selecting alternates), and more especially in view of the general situation and of the ordinary manner in which sensible business men conduct their affairs.

It is clear that Craig was designated as one of the escrowees primarily for assurance against any possibility of control of these funds without the approbation of the contractors who had deposited them. Craig was a secretary of the Building Construction Employers' Association of Chicago, a master association comprising lesser associations of one or more of which each of the contractors was a member. (Rec. 24.) The interveners allege that in the escrow matter Craig, Harris, and Odell, were acting as representatives of the interveners and

of their various associations. (Rec. 28.) Craig's answer states: "* * * that he was not acting at any time as the agent or representative of and had no connection with the Tax Service Association of Illinois."

It is interesting to note in connection with the allegations of the interveners' petition, and in connection with the subsequent desperately devised contention of the interveners; that the escrowees or some of them were agents of the alleged bankrupt, that the interveners allege under oath that they "requested Benjamin F. J. Odell to cease from acting as attorney or representative of the petitioners", (respondents), (Rec. 31), and that they "requested R. G. Harris to cease from acting for or representing any of the petitioners" (respondents). (Rec. 32.) It is significant that at that time, before they realized the jurisdictional demands made upon their "facts", they regarded Harris and Odell, as well as Craig, as *their* representatives, or more accurately trustees.

In the case of *Seibel* v. *Higham*, 216 Mo. 121, 132; 115 S. W. 987, the court said:

> "* * * The depositary of an escrow is sometimes spoken of as the agent of the grantor and sometimes as the agent of both parties, and whilst that may be correct, in a limited sense, yet strictly speaking he is not an agent at all, he is a trustee of an express trust with duties to perform for each which neither can forbid without the consent of the other, * * *."

While it may be argued that Harris was an officer of the alleged bankrupt, it cannot be disputed that he was acting in his own individual capacity as trustee of the escrow fund. See: *St. Paul's Episcopal Church* v. *Fields*, 81 Conn. 670, 72 Atl. 145. *Bowman* v. *Brown*, 87 N. J. Eq. 47 at 48. 99 Atl. 839. Although petitioners

were given no opportunity to be heard on the facts with respect to the relations of the various parties, it seems inconceivable that a fair-minded person could draw from the present record any conclusion other than that the three escrowees were trustees, and not agents of the alleged bankrupt.

4.

There was neither actual nor constructive possession within the meaning of such terms as used by the authorities.

Overlooking solely for the purpose of argument the fact that the present controversy does not relate to the estate of the bankrupt, it is submitted that there was no such possession as would support the jurisdiction of the bankruptcy court, nor was the property of such character as could be "possessed" in this sense.

Here the property was not in the custody or control of the receiver, as evidenced by the fact that on June 3rd, 1937, (seven days after the "agreed" order), the receiver filed a petition asking that part of the funds be held until adjudication. (Rec. 53.) Obviously such request would have been unnecessary had there been possession or control by the court's officer.

The contention of respondents that there was possession predicated upon the assumption that the three escrowees were agents of the alleged bankrupt falls, of course, with the demonstration above made of the fallaciousness of that assumption.

In the case of *Buss* v. *Long Island Storage Warehouse*, 64 Fed. (2d) 338, 340, the bankruptcy court laid down the doctrine that where possession by an agent of the bankrupt is relied upon as the basis of summary jurisdiction, the agent and the property must be *uncondition-*

ally subject to the bankrupt's orders. The Court said on page 340:

> "* * * As we have said, the underlying notion is that for jurisdiction to attach, the bailee must be unconditionally subject to the bankrupt's orders * * *"

See also *Sproul* v. *Levin*, 88 Fed. (2d) 866 (C. C. A. 2).

In the case at bar, there was certainly no unconditional control granted the bankrupt over the escrow fund. As a practical matter, even if Harris had been its agent, the bankrupt could have exercised no domination whatever over the fund without the written consent of both Craig and Odell. No one or two escrowees controlled the fund. (Rec. 27.) This utter lack of possession or control of the fund by Harris, let alone the alleged bankrupt, was completely overlooked by the Circuit Court of Appeals.

It is further submitted that the funds were of such a character that they were not property even *capable* of being in the possession of the bankrupt or its agents. Assuming that there had been a bankruptcy trustee as distinguished from a receiver who gets no title and consequently is unable to maintain a proceeding, the most that would have inured even to such trustee would have been a mere chose in action. It is clear that the relationship between the depositary bank and the escrowees is that of debtor and creditor, and hence all that the escrowees had was a mere chose in action. It is equally apparent that any claims against them with respect to this escrow, including any claim which the alleged bankrupt might have, could not be more than a chose in action. The liquidation of such chose in action would necessarily require extensive litigation, and the determination of many complicated questions of law and fact.

A chose in action is not property which may be in the possession of a bankruptcy trustee, so as to support jurisdiction.

Board of Trade v. *Johnson*, 264 U. S. 1.
Kelley v. *Gill*, 245 U. S. 116.

The tenor of these last two cases is well indicated by the following language which appears on page 121 of the *Kelley* case:

> "Nor can the jurisdiction of the court of bankruptcy be maintained on the ground that this is a suit brought to determine a controversy concerning property in the possession of the trustee. He had possession merely of contested claims against alleged stockholders. * * *"

In the case of *In re Roman*, 23 F. (2d) 556, page 558, the Court said:

> "* * * The trustee must proceed as the bankrupt must have proceeded, in a court having competent jurisdiction in such causes. This was clearly the distinction which the court had in mind in *Board of Trade* v. *Johnson*, 264 U. S. 1; 44 S. Ct. 232, 68 L. Ed. 533, where the decision turned entirely upon whether a seat in a trading exchange was property or a chose in action, and where the decision depended upon the view that it was property. Where procedural questions are at stake, such differences go to the essence, and we could not affirm the order without vesting in the bankruptcy court power summarily to try actions in contract, at least so far as to decide whether the defense is real."

As is clearly stated in Remington on Bankruptcy, Vol. 5, Fourth Edition, paragraph 2368, page 566:

> "Mere rights of action for money judgments or decrees in *personam*, and for debts owing to the bankrupt, etc., where no tangible property is involved, cannot well be said to constitute property

in the bankrupt's possession at the time of bankruptcy and therefore it would seem that the bankruptcy does not necessarily draw litigation, in relation thereto, into the forum of the bankruptcy court, although, of course, the bankruptcy court may issue injunction for the protection of contract rights. * * *"

It thus being demonstrated that the bankruptcy court had neither actual nor constructive possession of the funds in question it could not take jurisdiction of the intervening matter upon any possessory theory.

5.

Mere constructive possession is not sufficient to confer upon the bankruptcy court jurisdiction over a reclamation suit.

"Reclamation" proceedings are summary proceedings brought by third persons *against* the trustee to recover property wrongfully in the possession of the trustee. A "turnover" proceeding is a proceeding *by* the trustee to compel the bankrupt or a third party to "turn over" to the trustee property definitely in possession or under control of the bankrupt. Conceding, solely for the sake of argument upon this point, that the facts would have sustained jurisdiction of a "turnover" proceeding by the trustee (had there been a trustee) to reach the property for the benefit of the estate, still the facts would not sustain jurisdiction for a reclamation proceeding.

The reasoning of the Circuit Court of Appeals, and their construction of the case *Page* v. *Arkansas Natural Gas Corporation*, 53 Fed. (2d) 27, was directed to the proposition that something less than *actual* possession of the property in litigation was sufficient to sustain jurisdiction. The Circuit Court of Appeals, in concluding that

the funds in litigation were "so closely connected with its [bankrupt's] affairs", assumed that constructive possession was sufficient to sustain jurisdiction. Conceding the accuracy of the proposition that constructive possession is sometimes sufficient to sustain jurisdiction, nevertheless its application is limited to "turnover" proceedings, or proceedings in the nature of "turnover" proceedings brought by the trustee for the benefit of the estate. All cases sustaining the above proposition are not "reclamation" proceedings, but "turnover" proceedings. It is true that the case principally relied upon in the opinion of the Circuit Court of Appeals, *i. e., Page v. Arkansas Natural Gas Corporation* started out as a reclamation proceeding. However, the relief appealed from was granted upon the trustee's cross petition, which was clearly in the nature of a "turnover" proceeding, *i. e.*, to compel the execution of a quit-claim deed to the trustee.

On the other hand, with respect to reclamation proceedings, it is observed that *actual* as distinguished from *constructive* possession is not only contemplated, but indispensable for the jurisdiction. "Reclamation" proceedings have been evolved for the purpose of permitting a third party claiming property to recover the same from the actual possession of the bankrupt, his receiver, or trustee. When property is in the actual possession of the bankrupt, receiver, or trustee the only way to recover it is by a reclamation proceeding. Where, on the other hand, the possession of the trustee is merely constructive, as where for example, the property may have been removed without proper authority from the estate of the bankrupt, but is actually in the possession of a third party, other than the rightful owner, a reclamation proceeding would not only be unnecessary, but would not be

the normal remedy. The normal remedy then would be a replevin suit or other appropriate direct proceeding in an ordinary court of law or equity against the party actually in possession of the property.

There are a number of cases which hold that under the factual situation above outlined, *i. e.*, where property has been wrongfully removed from the possession of the bankrupt, that such property is in the constructive possession of the trustee, and may be recovered by him in a "turnover" proceeding conducted in the bankruptcy court. Obviously, "turnover" proceedings are proper to recover property in the *constructive* possession of the trustee; there would ordinarily be little occasion for such proceedings, however, where the property was in his actual possession.

A further broad distinction relevant to the facts of the present controversy exists between "turnover" and "reclamation" procedings. The former are always brought for the benefit of the estate; the latter, for the benefit of the third party instituting the same. There is every reason logically and legally why the constructive possession fiction should be indulged to confer jurisdiction upon a court of bankruptcy of a proceeding which benefits the creditors, the parties primarily sought to be benefited by the creation of such courts; there is very little reason, if any, why such a fiction should be indulged for the purpose of assuming jurisdiction to assist third parties, for the benefit of whom such courts were not created. Where the court has actual possession through its officers, no fiction is involved. Allowing reclamation proceedings under such circumstances constitutes no more than plain, fair dealing on the part of the court in turning over to such claimant property rightfully belonging to him, from the courts own possession.

The true basis of reclamation proceedings is aptly enunciated in *Murphy* v. *Hofman, et al.,* 211 U. S. 562, 568-9:

> "* * * But where the property in dispute is in the *actual* possession of the court of bankruptcy there comes into play another principle, not peculiar to courts of bankruptcy, but applicable to all courts, Federal or State. Where a court of competent jurisdiction has taken property into its possession, through its officers, the property is thereby withdrawn from the jurisdiction of all other courts. The court having possession of the property, has an ancillary jurisdiction to hear and determine all questions respecting the title, possession or control of the property. In the courts of the United States this ancillary jurisdiction may be exercised, though it is not authorized by any statute. The jurisdiction in such cases arises out of the possession of the property and is exclusive of the jurisdiction of all other courts, although otherwise the controversy would be cognizable in them. *Wabash R. Co.* v. *Adelbert College* 208 U. S. 38, 54. * * *"

Reclamation proceedings have developed by analogy to the law of replevin, it has been held that a reclamation proceeding cannot be maintained except under those circumstances and upon proof of those facts which would be necessary to maintain replevin or trover.

> Remington on Bankruptcy, 4th Ed., Vol. 5, Paragraph 2451, page 710; citing *Levi* v. *Picard,* 148 Fed. 654.

Inasmuch as the subject matter of the present controversy is merely a chose in action, it is obvious that neither replevin nor trover would lie here. See: *Spear* v. *Arkansas Bank,* 111 Arkansas, 29.

> "The right to reclaim exists only where the relation is that of bailor and bailee, not that of debtor and creditor."
>
> Brown's Guide to Federal and Bankruptcy Practice (1933), Par. 290, page 207.

Hence, it follows that the instant facts cannot possibly sustain a reclamation suit.

Thus the present controversy cannot be sustained as a reclamation proceeding because there was no actual possession of the property in the bankrupt.

6.

The petitioners did not in fact consent to the jurisdiction of the bankruptcy court.

Assuming that jurisdiction could be conferred by consent, it follows that such consent must be actual and not merely colorable. Such consent must represent a state of mind and not a mere metaphysical technicality. While it is true, of course, that a state of mind must be determined from overt acts, and that intention with respect to a written instrument must be gathered primarily from the language used, yet it is clear that such overt acts and such language must be construed and evaluated as a whole, and against the background in which they occur. Such intention is not to be determined merely from one overt act or one phrase where such act or phrase is clearly contrary to the actual intention of the parties as demonstrated by an entire course of conduct or written instrument as assessed against its background. Particularly is this true where as in the present case one party intentionally and deliberately attempts to make it appear that there was waiver of objections to jurisdiction when in fact all parties understood that there was no such waiver. (Rec. 93-4.)

No other fact in this case is quite so clear as that from the ne petitioners were brought into this proceeding, both before the court, before the referee, and in

discussions out of the presence of the court, petitioners staunchly and consistently denied the jurisdiction of the court.

It is submitted that the so-called "agreed" order was entered under the worst type of coercion and compulsion to which conscientious parties, subject to a sacred trust, can be subjected. The Avery Brundage petition was filed on May 24, 1937. June 1, 1937, was the "deadline" for the payment to the Illinois State Department of Finance of taxes from the escrow fund in order to avoid the imposition upon and accrual to the interveners of heavy penalties in excess of $100,000. This fact was known to all parties concerned. Immediately upon the filing of the Avery Brundage petition, these petitioners took the position that the court was utterly without jurisdiction to entertain the same. This fact also was known to all parties. Petitioners were deeply cognizant of the duty which they owed to the beneficiaries of the Sales Tax Escrow Fund, and of the urgency of release of the 75% of this $314,000 fund by June 1, 1937. All parties were agreed that such funds should be released; however, they were not agreed upon the mode of their release. The attorney for the interveners (now for respondents) insisted upon an agreed order; the court refused to authorize the disbursement except upon such agreed order.

The nature of the duress practiced here could well be likened to the situation of a man with a jewel on the brink of a cliff threatening to cast the stone into the sea below unless his exactions of a promise be complied with by the owner of the precious gem. The promise made under duress, to save the jewel, cannot be enforced.

The funds would have been largely destroyed by imposition of heavy penalties unless 75% of the funds could

have been disbursed promptly. The attorney for respondents here knew well the necessity for such disbursement, and deliberately "tied up" such funds, to prevent disbursement except upon his own terms one of which terms was these petitioners sign the so-called "agreed" order.

The intervention into the bankruptcy proceeding was so audacious and unprecedented that the court felt the need for additional time to consider the question of its own jurisdiction. That the court doubted its own jurisdiction even then is aptly indicated by the language of the Circuit Court of Appeals:

> "* * * It would seem the court, at that time, might have been somewhat dubious of the situation, as each party in interest, either personally or by attorney, was required to and did approve said order in writing." (Rec. 132.)

Inasmuch as Craig, the third escrowee, and the National Builders Bank had also been made parties to the intervening petition, and were unwilling to take a chance and disburse the funds without an order of the court, it is obvious that such disbursement could not be made without that order. It is now clear that the bankruptcy court then in fact had no jurisdiction. Hence, it follows that the restraint imposed upon the disbursement was wholly without authority. The duress thereby imposed vitiated any apparent consent to the jurisdiction. That duress may be imposed by the unauthorized assumption of jurisdiction can hardly be questioned. When a judge assumes to entertain a proceeding over which he is utterly without jurisdiction, he is acting as any other private person and not as a court. The mere fact that the judge was honestly mistaken and was unwittingly imposed upon by counsel for respondents in the pursuance of his devious plans, and as a result of such mistake allowed the petition to be filed, is of course immaterial.

The foregoing is based upon the assumption that petitioners did purport to consent to the jurisdiction of the court in the so-called "agreed" order. An examination of the "agreed" order, however, discloses that even this assumption is unfounded.

To what did petitioners agree? They agreed that the "court" had "jurisdiction to enter this order." What jurisdiction was required "to enter this order"? To answer this question it is necessary to determine the effect of the order. Its sole and total effect was merely an authorization by the court to your petitioners, to Craig, and to the bank, to disburse 75% of the funds. It was merely permissive, and had no mandatory force or effect.

While it may be contended that jurisdiction to dispose of the balance of the fund was approved because the order provided "that the balance of the money in said Sales Tax Escrow Fund * * * shall remain and be held in said Escrow Fund in the National Builders Bank of Chicago subject to the further order of this court", it is believed that slight consideration will indicate this language was wholly nugatory. The language certainly does not indicate consent to any change in the status of the escrow fund or in the quantum of control or jurisdiction of either individuals or court over it. The language is that the balance "shall *remain* and be held * * * subject to the further order of this court," not that it shall *become* subject. Certainly "remain" indicates continuation of the existing situation, *i. e.*, that it "shall remain * * * subject" to the order of the court in the sense that, and to the extent only that, it was "subject" before the order was entered, *i. e.*, that the escrowees and the bank could not disburse the balance until the court made a further order. Was not the fund "subject" to the order of the court in this sense prior to the entry of the agreed

order? Certainly the bank, to say nothing of the escrowees, would not have permitted the funds to be withdrawn in the face of the intervening petition without some court order.

It must also be noted that the provision was that the balance of the fund should remain subject to the further "*order*" of the court; not that it should be subject to the *jurisdiction* of the court. An order of the court dismissing the intervening petition for want of jurisdiction would constitute such further "order".

It was just such an order which the court should have made. At the time the "agreed" order was entered, all parties anticipated and understood that such "further order" should be an order determining the question of jurisdiction. At the time of the entry of the order, it was insisted by these petitioners and agreed in open court that the consent requested by the court to such distribution would not prejudice their rights to have determined the question of the jurisdiction of the court over the 25% balance of said fund (Rec. 93-94, 62). That the court so understood the agreement is evidenced by the fact that the order itself gave these petitioners the right to file "their answer *or other pleadings* to said petition (Avery Brundage or first petition,) * * * to and including June 3, 1937." What is meant by "other pleadings"? Clearly the expression as herein used is broad enough to include, and was intended to include, pleas to the jurisdiction.

The agreement reserving the right to object to the jurisdiction was urged upon the trial court in the exceptions filed to the referee's report in the following language:

"* * * It was at the solicitation and suggestion of the court that said 75 per cent of the funds were

distributed to the Department of Finance for the various petitioners in order to avoid a penalty against said petitioners for failure to pay said taxes within the allotted time, and it was stated by respondents and agreed to in open court that the consent requested by the court to such distribution would not prejudice the rights of respondents to have determined the question of the jurisdiction of the court over the 25 per cent balance of said funds." (Exceptions to referee's report (Rec. 93-94).)

That there were such agreements and understandings that objections to the jurisdiction should not be waived by consent to the so-called "agreed order" is evidenced by the following language from the report of the referee in the bankruptcy matter, (Rec. 62):

"Attorney Sigmund W. David of the law firm of David & Fainman, which law firm had filed the so-called Avery Brundage Company, *et al.*, petition, stated at the hearing before me that, in fairness to the attorney for the alleged bankrupt corporation, he thought he should state that it was the understanding between Attorney Flaherty (attorney for the receiver), the attorney for the alleged bankrupt corporation and himself that the so-called Avery Brundage Company, *et al.*, order was entered subject to the then pending motions of the alleged bankrupt corporation to quash the service. He further stated that the original draft order which he drew said something about it, but it was thought unnecessary, as it was felt that the order in relation to the so-called Avery Brundage Company, *et al.*, petition would not affect the then pending motion of the alleged bankrupt corporation on the question of service and jurisdiction."

A somewhat similar situation arose in the case of *Frank* v. *Vollkommer* decided by this court in 205 U. S. 521. There the parties agreed to the sale of certain property by the bankruptcy receiver and agreed that the proceeds be deposited in a bank *"there to await the further order of the court."*

In subsequent litigation in the State Court it was argued that there was no jurisdiction in the State Court because the propery was in the custody of the bankruptcy court. This court, upon appeal denying that contention, said on page 528:

> "The contention is wholly inadmissible. The mortgaged property consisted of horses, vehicles, harness, etc., and the order of sale of the temporary receiver, agreed to by plaintiffs in error, was evidently in the interest of all parties, and provided for the deposit of the proceeds, not in the general funds of the estate, but as a special fund, to which the lien, if any, of the chattel mortgage was transferred, and clearly contemplated a plenary suit to determine the validity thereof, which, at that time, there being no diversity of citizenship, and no such possession as might lead to a different result, could only be commenced in the state court. * * *"

Thus it is demonstratd in case at bar that no actual consent to the jurisdiction of the court was given.

7.

Consent cannot confer jurisdiction of the subject matter, i. e., jurisdiction on the bankruptcy court of a controversy between strangers to the bankruptcy proceeding.

In the early case of *Olds Wagon Co.* v. *Benedict*, 67 Fed. 1, 5 (C. C. A. 8, 1895), the court used language now universally concurred in by the courts:

> "* * * No consent, agreement, or estoppel can confer jurisdiction upon a federal court to hear or determine any case in which the essential jurisdictional facts do not appear from the record. These rules are fundamental. They are settled by repeated adjudication of the Supreme Court, * * *"

In the case of *Nixon* v. *Michaels*, 38 Fed. (2d) 420, above discussed, a case in which the facts were almost identical

with case at bar, the court used the following significant language on pages 422, 423:

"(2) The question of jurisdiction was not raised directly in the court below; nevertheless, it is the duty of this court to determine the question. *M. C. & L. M. Ry.* v. *Swan*, 111 U. S. 379, 382 * * *; *C. B. & Q. Ry. Co.* v. *Willard*, 220 U. S. 413, 419, * * *; *B. & O. R. Co.* v. *City of Parkersburg*, 268 U. S. 35, * * * *Highway Const. Co.* v. *McClelland*, 14 F. (2d) 406 (C. C. A. 8)."

"(3) A District Court of the United States sitting as a court of bankruptcy is a court of limited jurisdiction. Limitations exist as to subject matter; as to territory; as to the residence and occupation of the debtor to be adjudicated; as to the status of the corporation or person to be adjudicated; and as to other matters. Remington on Bankruptcy (3rd Ed.), c. III. And consent cannot confer jurisdiction over subject matter. The express provisions of the statute and the necessary implications are controlling. Id. p. 66; *Bardes* v. *Hawarden Bank*, 178 U. S. 524, 535, * * *; *Henrie* v. *Henderson* (C. C. A.), 145 F. 316, 320; *Nelson* v. *Svea, etc., Co.* (D. C.), 178 F. 136, 140; *In re Hollins* (C. C. A.), 229 F. 349; Id. (C. C. A.), 238 F. 787; *Jones* v. *Kansas City, etc., Co.*, 1 F. (2d) 649 (C. C. A. 8); *In re Judith, etc., Co.* (C. C. A.), 5 F (2d) 307."

The United States Supreme Court has consistently held that lack of Federal jurisdiction cannot be cured by consent.

"Third. Unlike an objection to venue, lack of Federal jurisdiction cannot be waived or be overcome by an agreement of the parties. An appellate federal court must satisfy itself not only of its own jurisdiction, but also of that of the lower courts in a cause under review. * * *"

Mitchell v. *Maurer*, 293 U. S. 237, 244.

Flanders v *Coleman*, 250 U. S. 223, 228.

Hancock v. *Holbrook*, 112 U. S. 229, 231.

Mansfield, etc. Railway v. *Swan*, 111 U. S. 379, 382-4.

That the bankruptcy court did not have jurisdiction of the subject matter, has been demonstrated. The courts have held that federal grounds of jurisdiction must appear on the face of the pleadings and not upon matters which may subsequently develop in the course of the trial.

Mosher v. *City of Phoenix*, 287 U. S. 29.
Barnett v. *Kunkel*, 264 U. S. 16.
Flanders v. *Coleman*, 250 U. S. 223.
Press Publishing Co. v. *Monroe*, 164 U. S. 105.
Hanford v. *Davies*, 163 U. S. 273.
Oregon Short Line Ry. Co. v. *Skottowe*, 162 U. S. 490.
Dowl v. *Applegate*, 152 U. S. 526.
Colorado Central Mining Co v. *Turch*, 150 U. S. 138.
Metcalf v. *Watertown*, 128 U. S. 586.

What jurisdictional facts are required in the federal court? In law and equity suits allegations of requisite amount involved, diversity of citizenship, or other grounds of federal jurisdiction are imperative. Failure to allege these requisites has been held fatal. In a bankruptcy proceeding the allegations should specifically state the grounds upon which the jurisdiction of the court is invoked.

The requirements of a petition for reclamation are aptly stated in *Loveland on Bankruptcy*, Vol. 1, Page 853:

> "The intervening petition should state the date of filing the petition in bankruptcy, the adjudication, the appointment of the trustee or receiver, and that the property in question is in the possession of the trustee or receiver as a part of the bankruptcy estate."

It is significant that *neither petition* in case at bar contains an allegation of the fact that a petition in bank-

ruptcy had been filed against the alleged bankrupt. It contains neither the date of the petition in bankruptcy, the date of the appointment of the receiver, nor statement whether or not there are sufficient creditors; it is bare of any allegation with respect to the fact of adjudication, or lack of adjudication. (There had been no adjudication.) A stranger reading the petition would have no conceivable means of knowing that a bankruptcy proceeding was pending. Strangers were made parties to the proceeding,—the bank, E. M. Craig, Benjamin F. J. Odell and Roy G. Harris. It contains no allegations of diversity of citizenship, nor any other facts which might support jurisdiction.

The Statute is clear:

> "If in any suit commenced in a District Court, * * * it shall appear to the satisfaction of the said District Court at any time after such suit has been brought * * *, that such suit does not really and substantially involve a dispute or controversy properly within the jurisdiction of said District Court, or that parties to said suit have been improperly or collusively made or joined, either as plaintiffs or defendants for the purpose of creating a case cognizable * * * under this chapter, the said District Court, shall proceed no further therein, but shall dismiss the suit * * *, as justice may require, and shall make such order as to costs, as shall be just."
>
> United States Code, Title 28, Chap. 3, Sec. 80.

Even though the petition contained allegations sufficient to sustain its filing in the bankruptcy court, with reference to the existence of a bankruptcy matter, still petitioners contend that the intervening petition is fatally defective. In neither the first nor the second petition is there any allegation that the funds were in the custody and control of the bankrupt. On the contrary the first petition reveals that the funds were under the control

of Craig, Harris and Odell (Rec. 27). Respondents state that they requested Odell to sign a check, but that he refused, and that the same request was made of Harris (Rec. 31-3). They requested both Harris and Odell to cease from acting as their representative or agent (Rec. 31-3). They say that respondents need the money to pay the sales tax. No offer is made to do equity, to pay Odell for his services as an attorney covering two years of complicated and protracted litigation, but they say that neither Harris, Odell, Tax Service, nor anyone else is entitled to any of the money (Rec. 28). The prayer is not that the Tax Service turn over the money in the fund, but that three strangers to the proceedings sign a check upon a bank which likewise is a stranger to the proceeding, and make the check payable to three other strangers. Such a bill would have been fatally defective in any proceeding.

Defective as the first petition may have been, the second petition, the one relied upon here in this controversy, presents not a single ground of bankruptcy jurisdiction. We challenge respondents to point out to the court a single allegation which states either directly or indirectly that the funds were subject to the control of the alleged bankrupt. Not one valid reason is presented why the bankruptcy court should assume jurisdiction to enter the orders appealed from.

The law is too well settled for dispute that to justify the stringent demands of the Statute above quoted an absence of any of the allegations of jurisdiction from the pleadings makes it mandatory for the District Court to dismiss the cause of action. The Court should have looked beyond the ill-concealed attempt of respondents to transform a petition in equity into a bankruptcy controversy, by merely filing it in the bankruptcy court and

without alleging any facts which would justify the court in determining the question. If the jurisdiction be sustained, no logical reason exists why a divorce action, for instance, could not be similarly prosecuted in a bankruptcy proceeding. The mere fact that a bankrupt entered into a contract with certain associations, and that its vice president happened to be one of three escrowees of certain funds, does not license the bankruptcy court to hear and determine disputes with reference to the amount of taxes escrowed by numerous individuals.

Consent cannot confer upon courts powers withheld by statutes and the constitution. Consent cannot transform an ordinary bill in equity into a bankruptcy controversy.

In *Metcalf* v. *Watertown*, 128 U. S. 586 at 589, this Court said:

> "* * * Where, however, the original jurisdiction of a Circuit Court of the United States is invoked upon the sole ground that the determination of the suit depends upon some question of a Federal nature, it must appear, at the outset, from the declaration or the bill of the party suing, that the suit is of that character; in other words, it must appear, in that class of cases, that the suit was one of which the Circuit Court, *at the time its jurisdiction is invoked, could properly take cognizance.* If it does not so appear, then the court, upon demurrer, or motion, or upon its own inspection of the pleading, must dismiss the suit; just as it would remand to the state court a suit which the record, at the time of removal, failed to show was within the jurisdiction of the Circuit Court. It cannot retain it in order to see whether the defendant may not raise some question of a Federal nature upon which the right of recovery will finally depend; and if so retained, the want of jurisdiction, at the commencement of the suit is not cured by an answer or plea which may suggest a question of that kind. * * *" (Italics ours.)

In the case of *Barnett* v. *Kunkel*, 264 U. S. 16 at page 19-21 we find:

> "No question of our jurisdiction to hear this appeal is raised by the appellees. That, however, does not relieve us from the duty of inquiring into it. * * * The complainant in deraigning his title disclosed the fact that it rested on the allotment of the land in question to a deceased Creek Indian minor, that the land was inherited by the minor's mother and was conveyed by that mother as a full blood Creek Indian with the approval of the County Court, all in accordance with and by virtue of a law of Congress; but there was nothing to show on the face of the bill that the validity of this conveyance was questioned under that law. The averment that the defendants were asserting a conflicting title or interest did not show that the issues which the assertion of their claims would present for trial, would necessarily involve the validity of the conveyances made under and by virtue of the Federal law, any more than the legal sufficiency of the many other conveyances set forth in the bill in the chain of complainant's title. It is true that the issues made by the answer clearly involved a consideration and construction of the effect of the Federal Statute of May 27, 1908. And perhaps others, but that fact subsequently developed would not furnish a ground for jurisdiction of a Federal District Court. In *Florida Central R. R. Co.* v. *Bell*, 176 U. S. 321, (p. 327), is was said:
>
> "It must be regarded as conclusively established by our decisions that the jurisdiction of the Circuit Court must appear in the plaintiffs' statement of their case."
>
> "* * * nothing of this kind appeared in the bill, and the development of the real Federal issues in the answer or on the trial could not supply the defect in the original jurisdiction of the suit as one arising under the laws of the United States."

This court said in: *Flanders* v. *Coleman* (a bankruptcy controversy), 250 U. S. 223 at 227:

> "Whether the District Court has jurisdiction to

grant any relief must be determined upon a consideration of the allegations of the bill and the amendment thereto. * * *"

And on the bottom of page 228:

"The opinion of the District Court shows that it really considered the merits of the case in reaching the conclusion that it was without jurisdiction. As this court has not infrequently said, jurisdiction must be determined not upon the conclusion on the merits of the action, but upon consideration of the grounds upon which Federal jurisdiction is invoked."

Therefore, consent cannot confer jurisdiction of the subject matter where no grounds of federal jurisdiction appears from the record.

Point II.

The orders appealed from deprived petitioners of property without any opportunity whatever to be heard on the merits of the issues.

"Every litigant, of course, is entitled to an opportunity to be heard upon the merits of a suit to which he may be a party or interested."

Thus the Circuit Court of Appeals concedes petitioners' right to a hearing (Rec. 133). It could not, of course, do otherwise in view of the due process clause of the Fifth Amendment to the United States Constitution. Yet, although paying lip service to this principle, the Circuit Court of Appeals affirmed the orders of the District Court which denied petitioners their right to be heard, and thus the effect of the decision of the Circuit Court of Appeals is in and of itself a denial of that "due process" which the Fifth Amendment guarantees.

It is earnestly submitted that the right to be heard as

guaranteed by the constitution is a right of substance and not a mere technical right of which an honest litigant may be deprived by a technical contrivance amounting to little more than judicial chess.

From time immemorial the idea has been ingrained in the Anglo-American system of pleading that a party has the right to plead to the jurisdiction first, and subsequently, plead to the merits; that a party may refrain from pleading to the merits until questions of jurisdiction have been disposed of. This principle is so strongly instilled in our system of jurisprudence that, in the absence of statutory modification, a plea to the merits constitutes a waiver of jurisdictional objections, as concerns those objections which can be waived at all. In all events, it is beyond dispute that the Federal Equity Rules and General Orders in Bankruptcy under which the District Judge was proceeding, and by which he was bound, contemplate that a defendant or respondent in a bankruptcy court may plea to the jurisdiction, and shall have five days after such plea has been overruled within which to file his plea to the merits.

Rule 29 for Courts of Equity of the United States concludes as follows:

> "• • • If the defendant move to dismiss the bill or any part thereof, the motion may be set down for hearing by either party upon five days' notice, and if it be denied, answer shall be filed within five days thereafter or a decree *pro confesso* entered."

Rule 37 of Rules in Bankruptcy is as follows:

> "In proceeding in equity, instituted for the purpose of carrying into effect the provisions of the act, or for enforcing the rights and remedies given by it, the rules of equity practice established by the Supreme Court of the United States shall be followed as nearly as may be. In proceedings in law, insti-

tuted for the same purpose, the practice and procedure in cases at law shall be followed as nearly as may be. But the judge may, by special order in any case, vary the time allowed for return of process, for appearance and pleading and for taking testimony and publication, and may otherwise modify rules for the preparation of any particular case so as to facilitate a speedy hearing."

It is clear, of course, that this limited power of modification granted to the trial judge is not intended to include the right to deny a hearing. No "special order" or any other order for that matter, for time in which these petitioners could answer to the merits, was ever entered by the trial judge which purported to change the order of pleading contemplated by Federal Equity Rule 29. The Circuit Court of Appeals states:

"* * * On one occasion the court expressly directed them [the petitioners] to file an answer as to the merits, but this they refused or neglected to do." (Rec. 133.)

Doubtless the court here has reference to certain language contained in the order of June 29, 1937, which language when removed from its context might seem so to indicate, but concerning which more is said immediately hereafter.

On May 24, 1937, the first petition, the Avery Brundage intervening petition, was filed before the District Judge, sitting in Bankruptcy. On May 27, 1937, in an order agreed to by respondents, petitioners here were given until June 3, 1937, to file an answer "or other pleadings" to the said petition. On June 3, 1937, Harris filed a "Motion to Strike" the said petition for want of jurisdiction. On the same day Odell filed similar pleadings. No hearing was ever held on the petitions and motions to strike so filed.

On June 29, 1937, respondents abandoned the so-called Avery Brundage petition, having then found that they did not represent Avery Brundage Company, (Rec. 69-70), and substituted therefor the so-called Dahl-Stedman petition.

The motions to strike as previously filed, were permitted to stand to the second petition (Rec. 74). The latter petition, together with the motions to srike were referred to the referee the same day they were filed, June 29, 1937 (Rec. 73-5). That order of reference was limited solely to the question of jurisdiction (Rec. 75). Other issues then pending were not referred to the referee (Rec. 46-53). Notwithstanding the restriction on the referee to hear and report on the jurisdictional question only, he reported on the merits even without having any hearing whatever on the merits, and found the allegations of the second petition to be true (Rec. 78).

In his report the referee referred to certain sections in the order of reference (Rec. 84, 85) in which it appears that petitioners here were asked whether or not they desired to answer the second petition. The order recites they responded that they did not desire to answer said petition but asked that the pleadings to the first petition stand to the second petition, and to which the court consented. The order is misleading. The statement that they wished to be heard first on the jurisdiction before answering to the merits was evidently misconstrued as a waiver of their rights to be heard later on the merits.

The order of reference was obtained under most unusual circumstances. Sigmund W. David, attorney for the intervening petitioners, presented said order of reference to the court in the absence of all other counsel and without their approval, and copies of the draft order

were not given to other counsel until the day after it was entered (Rec. 92). That reference order falsely related that petitioners here had stated they did not desire to answer the petition. At no time did they say they did not desire to answer the petition or to be heard on the merits. To the contrary they sought hearing on the merits which the court denied over exception (Rec. 96).

On July 7, 1937, the referee's report was presented to the court recommending the signing of a check by your petitioners for some $48,580 and further recommending that the National Builders Bank of Chicago honor and pay the same despite the fact the matter had not been referred to the referee on the bank's answer and the bank had not been present at the hearing nor had there been any hearing on the merits concerning the bank's or anyone else's pleadings.

In their exceptions filed to the referee's report, petitioners set forth that the order of reference dated June 29, 1937, stated erroneous facts and that the order was presented to the court in the absence of other counsel; that petitioners were desirous of having their motions to the jurisdiction disposed of before they answered to the merits and that they did not waive their right to plead to the merits; that the erroneous portion of said order had misled the Special Master, or referee, and as his report indicated, furnished the sole reason for his recommending that the prayer of the intervening petition be granted without your petitioners being given an opportunity to be heard on the merits (Rec. 92).

Those exceptions set forth many reasons why the Special Master's report should not be approved and the court's attention is directed to them on pages 92 to 95 of the Record.

The trial court sustained the Special Master's report, erroneous as it was, and thereby deprived petitioners of their right to be heard in court on the merits of the issues.

Had the court not arbitrarily denied the motion to file answers to the merits, it would have been informed of the following facts: That the funds involved in the petition were subject to an attorney's lien, as Odell had not been paid for the services rendered the contractors for engaging him and for whom he had been eminently successful, (*Blome Co.* v. *Ames,* 365 Ill. 456, 459; see also *Herlihy Mid-Continent Co.* v. *Nudelman,* 367 Ill. 600, 605); that intervener's petition was not actually the petition of all of the alleged interveners; that a liability existed if petitioners, as escrow officers or trustees, turned over the funds without special written request from each contractor or without an indemnity for so doing; that the contractors hired Odell by written contracts independent of the contract between trade associations and the alleged bankrupt, and that he is entitled to the wage of his hire; that there was an acceptance of the services of Odell and there was an express agreement to pay him; that there was an injunction in force in the State Court preventing distribution of the funds; (Rec. 169, 194); that on May 12, 1937, a restraining order of the United States District Court in this very case was entered in effect preventing the dissolution of the said injunction in the State Court and that it is still in full force and effect; (Rec. 195-6) that the further disbursing of said funds would be a violation of said injunctions; that there was no actual consent by petitioners to the jurisdiction of the court; that petitioners believe the intervening petitions were filed without authority and knowledge of many of the contractors for whom they purported to be filed; that other

contractors (not in this suit) have conflicting interests and rights in the fund. These and other important facts do not pass before the court for consideration upon a summary disposition of this cause on a mere jurisdictional plea, yet $48,580 involved was thus arbitrarily disposed of.

The portion of the opinion of the Circuit Court of Appeals dealing with the denial of the right to be heard on the merits, comprises only half a page, and with the indulgence of the court, we should like to set it out with our brief comments through the next few pages:

> "Every litigant, of course, is entitled to an opportunity to be heard upon the merits of a suit to which he may be a party or interested. * * * Appellants do not state, but intimate they have some interest in the funds in question. * * * If so, they should have asserted such claim." (Rec. 133.)

Petitioners submit that they have done everything humanly possible to assert such claim, but that right was denied them.

> "It cannot be said they did not have an opportunity to do so. On one occasion the court expressly directed them to file an answer as to the merits, but this they refused or neglected to do." (Rec. 133.)

The Circuit Court of Appeals has here followed the trial court's misconstruction of, and the misleading language in, the order of June 29, 1937, a matter concerning which we have above commented at length.

> "Even as to the $20,000 remaining in the fund, they were given permission as to the merits, but instead they appeal on the alleged jurisdictional matter. Under such circumstances they are in no position to here complain of the denial of a right which they could have availed themselves of, had they so desired." (Rec. 133.)

Here the Court no doubt has reference to the motion of respondents filed July 13, 1937, after the order disbursing the funds had been entered, which motion asked that petitioners' objections to the jurisdiction be stricken, and that these petitioners be required to answer as to remaining funds; also to the order of court entered in accordance with this motion, and to the answer of petitioners filed July 30, 1937, in which they informed the court that an appeal was being perfected and asking not to be required to answer until the appeal was disposed of. Obviously, it was not the intention to waive the right to plead to the merits, but merely to postpone the exercise of that right until the question of jurisdiction was determined, a postponement evidently acquiesced in both by the court and respondents, inasmuch as no further proceedings have been had with respect to that motion.

> "What interest in this fund they might assert, we do not know, but we are convinced from an examination of the record, they could have no interest or claim for services rendered in connection with the litigation in the matter of the sales tax, as the agreement betweeen appellees and the alleged bankrupt explicitly provided that such services were to be paid for by the latter and without cost to appellees." (Rec. 133.)

Little additional comment is required here. One side of the story only has been heard. Some estimate of the reliability of that one version may be made from what does appear in the record.

For example, despite the fact that both intervening petitions are verified, the second admits that the first was false in stating that Sigmund W. David was authorized to act on behalf of Avery Brundage Company. (Whether or not he is authorized to act upon behalf of all or any of the others, petitioners here have had no opportunity

to call upon him to demonstrate by a hearing on the merits.) Further, George V. Dahl, the affiant in both the intervening petitions, verifies under oath a form of contract purported to have been entered into by Odell and various respondents. There is set out in the appendix hereto a copy of the true contract, a radically different one, entered into between Odell and Dahl-Stedman Company, which contract is signed upon behalf of that Company by the same George V. Dahl as president. There are a great many facts in connection with this case which petitioners have been denied the opportunity to present.

The position of these petitioners, free from the intentionally misleading appearance of refusal to plead to the merits, is rather simple. The intervening petition is filed; these petitioners pleaded to the jurisdiction of the court to entertain it. On the same day that their plea to the jurisdiction was overruled, petitioners asked leave to plead to the merits; this right was denied. This right to plead to the merits was one to which they were entitled not only under the General Orders in Bankruptcy and the Federal Equity Rules, but guaranteed to them under the Fifth Amendment to the Constitution.

Point III.

The Circuit Court of Appeals and the trial court committed further errors requiring reversal.

The trial court, seemingly with the approbation of the Circuit Court of Appeals, committed other errors in its rulings which deprived petitioners of that due process to which every litigant is entitled, and which errors require reversal. The attention of the court is respectfully directed to the fact that although the errors hereinafter treated were pointed out to the Circuit Court of Appeals,

and urged as grounds for reversal, yet the Circuit Court of Appeals took no cognizance whatever of them in its opinion as far as that opinion indicates.

1.

The court erred in entertaining an involuntary petition against a corporation organized not for profit.

A taxpayers association organized not for pecuniary profit, is not within the purview of the Bankruptcy Act:

> "* * * Any unincorporated company, and any moneyed, business, or commercial corporation (except a municipal, railroad, insurance, or banking corporation, or a building and loan association) owing debts to the amount of $1,000 or over, may be adjudged an involuntary bankrupt upon default or an impartial trial, * * *."
>
> Title 11, Chapter 3, Section 22 (b) U. S. C. (Bankruptcy Act).

Inasmuch as the alleged bankrupt was a corporation "not for pecuniary profit" (Rec. 6, 9), and hence not a "moneyed, business or commercial corporation," the bankruptcy court had no jurisdiction whatsoever of the proceeding. It would follow from this that the court could not entertain an intervening petition with respect to a collateral controversy, the sole jurisdiction over which was predicated upon jurisdiction of the bankruptcy proceeding. Although the record does not disclose it, after denial of rehearing of this cause in the Circuit Court of Appeals, the Tax Service Association was adjudicated bankrupt; nevertheless the jurisdictional question over the subject matter is still subject to collateral attack.

2.

The court erred in determining an intervening controversy when its jurisdiction over the bankruptcy proceeding was in issue and undetermined.

The attention of the court is respectfully directed to the fact that in addition to the alleged bankrupt not being subject to the bankruptcy jurisdiction because not a "moneyed, business or commercial corporation", such alleged bankrupt had pleaded in good faith, contrary to the allegations in the petition, that it was not insolvent, and that it had committed no acts of bankruptcy.

It is submitted that the normal order of procedure for a court of bankruptcy having before it a petition for adjudication and collateral litigation, is to dispose first of the jurisdictional question of bankruptcy itself and to defer the determination of the collateral issue unless some good reason appears for a different order of proceeding. No such reason existed in the present case. To the contrary, justice urgently demanded the determination of the question of bankruptcy, whereas no reason whatever existed for hastening determination of the collateral issue which had existed in its present form more than two years—the time during which the funds in question had been held in the same depository in which they are now held. There had been no question raised as to the solvency of the bank. The funds were not likely to be wasted. No harm could possibly have resulted to any of the parties involved by the funds remaining in that bank until the question of the bankruptcy of the Tax Service Association had been determined.

As was said in *Woolf* v. *Reeves*, 65 F. (2d) 80, 82:

> "* * * It seems clear that the court should proceed no further than is necessary with the adminis-

tration of the estate in bankruptcy until the question of its jurisdiction is disposed of, * * *."

The Tax Service Association requested an immediate hearing on June 29th, but the matter was continued nearly three months, until September 21st. Petitioners cannot refrain from comparing this delay with the speed and facility with which the Sales Tax Fund litigation has been handled. The Dahl-Stedman, *et al.*, petition was also filed on June 29th, the day that the request was made for an immediate hearing on the bankruptcy matter. In connection with that petition, however, a reference was had; various motions were heard and summarily disposed of; a Referee's Report was filed; exceptions were filed and disposed of; and a final order upon these petitioners was entered on July 12th, exactly thirteen calendar days after the institution of the proceedings here appealed from.

It is earnestly submitted that the trial court erred in allowing counsel for respondents to rush this proceeding through the court, over the strenuous objections of petitioners; and that as a result of such haste the trial court allowed itself to be imposed upon and to be misled into assuming jurisdiction where it would have been apparent upon due consideration that none existed, and as a result of which haste the court was misled into denying to petitioners any opportunity to be heard upon the merits.

3.

The court disregarded Equity Rule 66 and denied petitioners sufficient time to file exceptions to the Special Master's report.

The court on July 9, 1937 (Rec. 91), ordered petitioners to file exceptions as to the referee's report within two days. The court was requested at that time to allow them ten days as provided by Rule 14 (Appendix, *infra*), of the Bankruptcy Rules of the District Court for the purpose of filing their exceptions to the referee's report. The trial court, however, took the position that the matter had been referred to the referee as a Special Master for the purpose of determining the issues in the petition. Thereupon these petitioners drew to the court's attention that (for Master's reports) under Rule 66 for Courts of Equity of the United States, petitioners should be allowed twenty days in which to file exceptions (Rec. 95). The trial court, however, insisted the matter should be summarily disposed of within three days and this, notwithstanding the fact that the hearing on the adjudication of the alleged bankrupt, over its strenuous objection, had been continued to the Fall. On the coming into court on the 12th day of July, 1937, petitioners again moved the court for a sufficient length of time in which to file their exceptions to the Special Master's report, which motion the trial court denied (Rec. 92). Thereupon they filed their exceptions to the report (Rec. 92), summarily and insufficiently prepared, in which, however, they briefly set forth the injustice done them in hurrying this matter and depriving them of a proper hearing.

RESUME AND CONCLUSION.

The present litigation constitutes a deliberate attempt to confer on a district court of the United States jurisdiction of a controversy over which it cannot have jurisdiction under the constitution, laws of the United States, and decisions of the Supreme Court. Neither of the intervening petitions stated a cause of action cognizable in any federal court, and even had your petitioners made no objection, both petitions should have been dismissed by the trial court upon its own motion, subsequently, by the Circuit Court of Appeals, and now ultimately by this court. The controversy is one between utter strangers to the bankruptcy proceeding, although respondents' attorney seeks desperately to connect your petitioners with the bankrupt by dubbing them "agents" of the bankrupt—contrary to the allegations of the intervening petitions themselves.

Jurisdiction cannot be sustained upon the theory that the bankrupt had possession of the fund, inasmuch as Craig, Harris and Odell were trustees. The funds could not be withdrawn from the bank without the order of Craig; it is nowhere even suggested that he was an agent of, under the control of, or in any way connected with the bankrupt. To the contrary, it is conceded he was not such agent. Jurisdiction cannot be sustained upon any theory of consent; there was no voluntary consent to jurisdiction in case at bar. Jurisdiction cannot be conferred upon a bankruptcy court in a non-bankruptcy matter with or without consent. Actual possession is indispensable for reclamation proceedings; in case at bar even constructive possession did not exist.

Unless this proceeding is reversed, there is no contro-

versy, jurisdiction of which cannot be conferred upon the federal courts by consent of the parties merely through the device of intervening in some pending bankruptcy proceeding.

The orders appealed from deprived your petitioners of property without any opportunity to be heard upon the merits of the issues. This right to be heard is a right of substance which cannot be "frittered" away by maneuvers of either court of counsel, and a right which a party does not forfeit, unless wilfully derelict in asserting it. At no time did petitioners waive that right. Instantly after the court had ruled adversely on the jurisdictional question, petitioners orally demanded a hearing on the merits, and within ten minutes that demand had been made a part of the record in writing.

The lower courts, in entertaining an involuntary petition against a corporation not subject to bankruptcy, committed further specific, substantial errors in law by determining prematurely an intervening controversy, and in denying proper time to file exceptions.

Ultimately, the situation is this: Your petitioners, along with one Craig, are trustees of a fund in which they have a substantial interest. Respondents herein seek to assert a claim against this fund by filing in a court, absolutely without jurisdiction, an intervening petition which containes no allegations upon which either jurisdiction or relief can be predicated. Counsel for respondents herein, through his kind of practice, not only persuades the District Court that it has jurisdiction, but prevails upon it to deny your petitioners a hearing on the merits. This unusual imposition upon the court is made possible by the fact that the trial judge allows the matter to be "jammed" through the court with such

haste as necessarily to preclude proper judicial consideration of the problems involved. Meanwhile, petitioners exercised full diligence to protect their rights, but diligence which seemingly is unavailing as related herein. Your petitioners are confident that this court will not tolerate such unwarranted assumption of jurisdiction and arbitrary denial of due process.

It is urged the orders of the lower courts appealed from be reversed.

Respectfully submitted,

BENJAMIN F. J. ODELL,
KENART M. RAHN,
Attorneys for Petitioners

APPENDIX.

Example of form of employment of attorney Odell used by some of the contractors:

"On the recommendation of The Builders Association, we hereby consent to the employment of Benj. F. J. Odell as our attorney to represent us in negotiations and litigation in an effort to change the present rulings of the Retailers' Occupation Tax Act as it applies to us, the expense in no event to exceed three months' savings of such taxes, payment of our share of the expenses to be made with the approval of The Builders Association under their agreement with said Odell as to a gross maximum fee. The above is subject to Bulletins issued by Mr. Craig dated April 17th and 23rd, 1935.

DAHL-STEDMAN CO.
GEO. V. DAHL,
(Seal) *As President.*

DAHL-STEDMAN CO.
ELMORE W. STEDMAN,
April 25, 1935. *As Sec'y. & Treas.*"
(Rec. 169-170.)

RULE 14.

"PETITION FOR REVIEW OF REFEREE'S ORDERS.

"The petition for review of a Referee's order shall be filed with the Referee within ten days after the order is made, unless, before the expiration of such period, the time be extended by the Court or the Referee in charge of the case. Where the order is the result of a decision upon a contested matter, the time within which to file the petition for review shall begin to run from the date of the service of a copy of the Referee's order upon the adverse party."

Bankruptcy Rules, U. S. District Court, Northern District of Illinois.